Before the U.S. Senate Committee on Banking, Housing and Urban Affairs
Written Statement of Irv Ackelsberg, Esquire
March 21, 2007

My name is Irv Ackelsberg. I am an attorney specializing in defending mortgage foreclosure and associated with the Philadelphia law firm of Langer and Grogan, P.C. I am also a member of the National Association of Consumer Advocates and I am on the board of the recently launched Americans for Fairness in Lending (www.affil.org). I retired last year, after 30 years of service, from Community Legal Services of Philadelphia, the nation's leading civil aid program.[1] I and my former colleagues at CLS have probably reviewed more abusive subprime transactions than any other law firm in the country. We are familiar with the practices of the companies that once dominated the subprime mortgage market, and the ones now in the news.

The subprime mortgage market has, for the last decade, grown at an astronomical rate. This growth has been fueled in large part by a collapse in underwriting practices and responsible lending principles; by a sales-pressured, get-rich-quick environment that has infected the market with blatant fraud and abuse, and a regulatory apparatus that has abdicated its traditional role to protect the American consumer from exploitive lending practices. In my view, and in the view of most consumer housing specialists, this fraud-infested market has been producing very little social benefit. While the particular abuses most prevalent are somewhat different than those we saw in the late 90's, the effects on the American homeowner have been steadily growing: unprecedented levels of foreclosures and equity-theft, all happening in full view of banking regulators.

At the ground level, from the standpoint of the America's neighborhoods, this growth in subprime lending has been the equivalent of a gold rush, where the gold being prospected is the home equity wealth of American homeowners. This gold rush has erupted because of the complete collapse in mortgage underwriting integrity. To put it bluntly, mortgage origination practices have been run over by the pursuit of profits at any cost. I want to describe for you some of this gold-rush-induced collapse in underwriting, but first I want to dispel two myths about subprime mortgage loans that the industry has been promoting.

First, it is not true that the typical subprime borrower is a low-income, first-time home-buyer purchasing his or her home. The majority of these loans are to existing homeowners who are being convinced to refinance their debt inappropriately. Sometimes the occasion for the transaction is a home improvement; sometimes runaway credit card balances drive the deal; sometimes the reasons for the loan are hard to discern. The bottom line is that if we want to look at these transactions as "opportunity" loans, the opportunity lies with the broker or lender profiting on the deal, not with the homeowner.

[1] CLS was, until 1996, funded by the Legal Services Corp. It had to give up that funding in order to avoid the restrictions imposed by Congress in 1996. Those restrictions would have prohibited much of my anti-predatory lending work.

The second myth is that these mortgages are credit-repair products. If that were true, most borrowers with subprime loans would be transitioning into prime products and the industry would essentially be lending itself out of existence. In fact, the opposite is the true. The subprime portion of the market has been steadily rising. Data gathered by researchers from The Reinvestment Fund on subprime lending in Philadelphia confirms that, particularly with low and moderate income borrowers, there is scant evidence of credit repair. On the contrary, there has been significant movement in the opposite direction, with borrowers in prime mortgage products transitioning into subprime.

The current abuses we are seeing include the following:

- Exploding adjustable mortgages with initial teaser rates that are underwritten to the teaser rate, not to the subsequent inevitable adjustment. This means that, at the time the loan is being made, there is no evidence of borrower repayment ability past the first two or three years of the loan.
- The widespread use of "no-doc", "stated" income loans.
- The absence of escrow for tax and insurance obligations which adds deception to the advertised payment and increases the likelihood of foreclosure.

In testimony I gave to the Federal Reserve Board last year, I called their attention to a sample securitization of New Century from the first quarter of 2006. Of the $1.4 billion of mortgage loans in that pool, only 10% were traditional 30-yr. fixed-rates, and an amazing 45% of those mostly adjustable-rate loans were "no-docs." The coming foreclosure crisis should not be a surprise to anyone, except perhaps for the magnitude. What we are seeing today, I believe, is a runaway train that is only starting to gather its speed. These recent foreclosures reflect large numbers of early payment defaults, that is, homeowners defaulting during the fixed-rate periods on their loans. We have yet to see the full effect of such a large share of outstanding mortgages starting to adjust upward. It is not unreasonable to predict as many as 5 million foreclosures over the course of the next several years. A number this high would represent one out of 15 homeowners in this country.

The inevitable question, then, is what can be done to reverse this course. We need to focus on constructing relief for those in trouble now and on imposing appropriate limits on the future lending practices of this industry. I have several suggestions.

In terms of addressing the coming foreclosure tsunami, we first have to recognize who is doing the foreclosures and why. It may be that the lenders testifying today have no interest in taking homes, but it is not the lenders who will be foreclosing. These loans are all made to order for Wall Street investors who purchase them almost immediately after they are created. Foreclosure decisions are made by massive servicing organizations that work for these investors. In the ordinary course of their business, these servicers never have to justify a quick foreclosure; they do, however, have to answer to their investors for any forbearance being offered to the borrowers. I believe that Congress will need to mandate moratoriums and debt restructuring in order to avoid a national disaster and to insure that the investors are absorbing some of the losses that otherwise will fall solely on America's homeowners. In the long run, however, the interests of financial markets and of homeowners are not in conflict: the downward spiral in property values that will be caused by massive foreclosures is something that only real estate speculators should wish to see.

As for civilizing this origination market gone amok, there are many sensible proposals that consumer advocates have been offering, such as imposing a suitability standard on mortgage-writing like what exists in the sale of securities, and imposing assignee liability on those who purchase these loans and fuel the market. On the latter approach, Congress already has used this tool effectively in the HOEPA legislation to successfully drive down the excessive points and fees that represented an earlier form of market abuse. Congress can and should take similarly dramatic action to curb these so-called "exotic" mortgages which, I submit, should be properly named "poisonous" or "irresponsible" mortgages. Actually, the Federal Reserve Board can do this on its own, using the "unfair and deceptive practices" authority that Congress granted the Board in HOEPA. And, finally, at the very least, Congress should let the states continue to make progress in this area and put to rest the specter of industry-sponsored, federal pre-emption.